DOCKET SECTION

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268

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Postal Rate and Fee Changes, 1997))) Docket No. R97-1

JOINT BRIEF OF ADVERTISING MAIL MARKETING ASSOCIATION, THE DIRECT MARKETING ASSOCIATION, MAIL ORDER ASSOCIATION OF AMERICA, ADVO, INC., SATURATION MAIL COALITION, NASHUA PHOTO, INC., DISTRICT PHOTO, INC., MYSTIC COLOR LAB, SEATTLE FILMWORKS, INC., VAL-PAK DIRECT MARKETING SYSTEMS, INC., VAL-PAK DEALERS' ASSOCIATION, INC. AND CAROL WRIGHT PROMOTIONS, INC. REGARDING REVENUE REQUIREMENT

The Advertising Mail Marketing Association, The Direct Marketing Association, Mail Order Association of America, Advo, Inc., Saturation Mail Coalition, Nashua Photo, Inc., District Photo, Inc., Mystic Color Lab, Seattle FilmWorks, Inc., Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealers' Association, Inc. and Carol Wright Promotions, Inc. (hereafter "AMMA, et. al.") submit this joint brief to address certain issues that have arisen concerning the Postal Service's revenue requirement. For the reasons set forth in this brief, AMMA, et. al. contend that the Commission should make its recommendations based on an FY 1996 Base Year and a FY 1998 Test Year, subject to adjustments to the revenue requirement based on the record as it stands. However, the Commission should also -- as a part of its decision -- state in the clearest possible terms the reasons why it believes the Board of Governors should defer implementation of the recommended rates until at least the end of this fiscal year and until it has been established that there is, in fact, a need for additional revenues.

In urging this outcome, we wish -- at the outset -- to make two points very clear. First, we, along with virtually all other parties to this case (and probably the Commission itself) are convinced that there is no need for the Postal Service to increase its rates immediately after the Commission issues its recommended decision as has been its historic practice, and the Postal Service probably will not need the additional revenues it seeks in this proceeding until the end of the fiscal year, at the earliest. Second, it is very clear that the "solutions" advocated by the OCA in this case to deal with this "embarrassment of riches" (OCA Brief at 9) cannot be adopted as a matter of law.

The solutions we advance recognize the first of these conclusions and avoid the legal infirmities of the second.

THE OCA'S REMEDIES ARE UNLAWFUL

The OCA advances two remedies to deal with the revenue requirement estimates. First, the OCA asserts that the Commission may "retain the First-Class 32 cent stamp rate" and impose "desired incremental rate increases for commercial mailers." OCA Brief at 20.

This argument presupposes that the better-than- expected performance in FY 1997 is <u>solely</u> the result of "non-commercial users" of the First-Class, first-ounce rate and that if in fact the Postal Service experiences "very large net profits" (OCA Brief at 20) in the Test Year, this, too, would be only attributable to revenues derived from the First-Class, first-ounce rate. There is no evidence to support this result. Still less is there any basis for distinguishing between "commercial mailers" and users of the First-Class, first-ounce rate. Commercial mailers of all classes -- no less than non-commercial users of the First-

Class, first-ounce rate -- have contributed very substantially to the better-than-expected performances of the Postal Service in FY 1997 and FY 1998. Thus, the OCA ignores entirely the cost and non-cost factors of Section 3622(b). This is something that the Commission manifestly cannot do.

The OCA's alternative remedy is that the Commission should recommend "no rate increase at this time." OCA Brief at 33. This recommendation is not based on the record, but upon the premise that the Governors "may choose to seek reconsideration" of such a recommendation and that the Commission would then have available accounting period data for all or a large portion of the remainder of the Test Year on which to update the record. Id.

One of a number of core difficulties with this approach is that the Governors may choose *not* to seek reconsideration. The Governors could choose to accept the Commission's recommended decision and the Board of Governors could then direct the Postal Service to immediately file a new rate case, using a Year 2000 Test Year and proposing rates very substantially higher than the indisputably moderate rate increases proposed here. It is difficult to see why the OCA believes that such a result would serve the interests that it seeks to protect; that result certainly would not serve the interests of AMMA, et. al. More importantly, the Commission should not permit ratemaking to become an exercise in power politics -- in which the Commission seeks to force the Governors to take steps that the Governors are not required to take under the statute. The OCA's remedy does violence to more than just the literal terms of the statute. It must be categorically rejected.

This does not mean that the Commission must blind itself to facts that came into existence after the case was filed, or simply accept the Postal Service's revenue requirement as originally filed. The OCA invokes a long line of cases for the proposition that "stale" data would endanger the validity of the Commission's decision. OCA Brief at 16. This is a principle which the Postal Rate Commission has recognized for many years and which the Postal Service does not seriously contest; indeed, Witness Porras proposes certain changes to the revenue requirement in his rebuttal testimony. See, USPS-RT-11 at Exhibit 11-C. However, neither the cases cited by the OCA nor Commission precedent allow for the wholesale substitution of data that the OCA urges here: adjustments to the revenue requirement must be made only to the extent permitted by and in the manner specified in the Commission's enabling statute and its own rules. Newsweek, Inc. v. USPS, 663 F.2d 1186, 1203-06 (2d. Cir. 1981); See, MOAA, et al. v. USPS, 2 F.3d 408, 429 (D.C. Cir. 1993).[1/]

Both of the OCA's proposals go considerably beyond adjustments of the type permitted in postal ratemaking and allowed under Commission precedent:

First, the FY 1998 data, even for the accounting periods that have been concluded, is preliminary and since that data represents approximately one-half of the Test Year, incomplete at best.

1/ The OCA reads the non-postal cases it has cited far too broadly. These cases deal with adjustments to an historic test year. By its rules, the Commission requires the Postal Service to use a forward looking test year which, by its very nature, entails reliance on forecasts. In addition, in each of these cases, the agency has final decision authority ovet the revenue requirement. In postal ratemaking the final decisional authority over the revenue requirement rests with the Governors. 39 U.S.C. §3621.

Second, the Commission itself has repeatedly stressed that its adjustments to the revenue requirement must involve recognition of post filing changes in both revenues and costs. See, e.g., Opinion and Further Recommended Decision in R90-1, Appendix I at 16-17. The state of this record will not permit the Commission, under its own precedent, to substitute actual FY 1997 data for the estimated FY 1997 data now in the record because the critical cost information -- the Cost and Revenue Analysis -- is not available.

Third, *even if the cost data were available and the Commission were therefore in a* position to in effect advance the Base Year from FY 1996 to actual FY 1997 or -- as the OCA seems to believe -- to the end of AP5 or 6 of FY 1998, the case would have to be tried all over again. The entirety of the record evidence concerning cost attributions, cost coverages, rate design and discounts is based upon an FY 1996 Base Year, the estimated Interim Year and the roll forward FY 1998 Test Year. Thus, unless an across-the-board rate reduction were possible, the parties would have to be given adequate time to analyze and challenge the actual FY 1997 data and any actual FY 1998 data used. MOAA et. al., 2 F.3d at 429. The statute does not give the Commission the power to waive the requirement that its proceedings be conducted on the record.

Accordingly, the Commission is not in a position to accept the OCA's recommendations. It can and should exercise its traditional responsibilities to update information in the record and make such modifications in the Postal Service's proposed revenue requirement as it can substantiate on-the-record. The Postal Service itself has proposed certain changes (including a reduction in the Prior Year Loss ("PYL") adjustment and the Commission has received testimony by intervenors -- including The Direct Marketing Association -- suggesting other record-based adjustments.[2/]

In making these adjustments, the Commission surely should accept the reduced PYL allowance. It may or may not accept Witness Porras' treatment of the contingency reserve. The contingency reserve proposed by the Postal Service in its original filing was lower than that proposed in any prior rate case. In its rebuttal testimony, Witness Porras increases the contingency reserve from 1% to 1.5%. In computing the revenue requirement, the Commission must allow some reserve for contingency, because the statute requires it. 39 U.S.C. §3621; see Newsweek, 663 F.2d at 1205.

However, even if the Commission rejects Witness Porras' adjustment of the contingency reserve, it still cannot lawfully reach either of the results contended for by the OCA. There is no basis in the record for a selective reduction of the First-Class first-ounce rates; and any on-the-record adjustment of the revenue requirement does not allow for an across-the-board reduction of all rates in a fashion which permits the Postal Service to break-even. Thus, the statute does not permit the Commission to use revenue results from FY 1997 and from the first five or six accounting periods of FY 1998 in the fashion proposed by the OCA.

2/ The adjustments advocated by The DMA are detailed in its brief.

THE COMMISSION CAN AND SHOULD URGE THE BOARD OF GOVERNORS TO DELAY IMPLEMENTATION OF THE RATE INCREASES

Nonetheless, there is a step the Commission can take that accords not only with the language but the purpose of the Postal Reorganization Act. The Commission can, in its decision, state that the Postal Service's Board of Governors should not implement the new rates until the facts show that the Postal Service needs the additional revenues.

No less than the Commission, the Governors of the Postal Service, appointed by the President with the advice and consent of the Senate, are bound by the terms of the statute. It is the Governors who have the ultimate duty to see to it that the Postal Service complies with Section 3621. This section expressly states that the "Governors are authorized to establish . . . equitable rates of postages and fees . . . . so that the total estimated income and appropriations to the Postal Service will equal as nearly as practicable total estimated costs of the Postal Service." Moreover, it is the Board of Governors which has the exclusive authority to determine when rate changes recommended by the Commission shall be implemented. Newsweek, 663 F.2d at 1204. The Governors simply do not have the unfettered discretion to ignore either the record or the realities associated with the Postal Service's ongoing performance and to implement rate increases before they are needed.

The exchange of correspondence between the Commission and the Board of Governors makes clear that the members of the Board of Governors are well aware of their responsibilities in connection with the revenue requirement. Although the Governors have not been as explicit as one might wish, their response to the Commission makes it clear that they are well aware of their power to defer implementation if, as in this case, there is no need for additional revenues at the time that a recommended decision is issued. Letter from the Chairman of the Board of Governors to The Chairman of the Postal Rate Commission (March 3, 1998).

In prior cases, the Board of Governors has taken heed of Commission advice concerning the Postal Service's revenue requirement needs. In particular, in Docket R94-1, the Commission accepted the Postal Service's revenue request for purposes of the rates it recommended in that case. Through 1994, the Postal Service had incurred "chronic operating losses" and the Commission pointed out that if this were to continue "future users of the Postal Service will subsidize current users." Decision in Docket R94-1 at II-32. It further observed that if rates were set to exceed operating costs until PYLs were fully amortized, it "would no longer be necessary to include such a provision in the revenue requirement." In dissent, the Vice Chairman stated that the Postal Service "has consistently under-estimated its revenue requirements." Dissent of Commissioner LeBlanc at 6.

The Governors took these concerns and criticisms to heart. The Postal Service has reduced its PYL in this case from $950 million to $377 million, as the result of its successful amortization of its so-called "negative equity." This represents nearly $600 million per year in savings to all users of the postal system, not just in the Test Year but in every year that the rates proposed by the Postal Service in this case remain in effect. The Commission's comments and the Governors' and Postal Service's response to those comments are exactly how Congress intended the statute to work.

The criticisms advanced by the Commission in R94-1 certainly do not apply here. The problem in this case is not that the Postal Service has "under-estimated its revenue requirements" (Dissent of Commissioner LeBlanc at 6). It is simply that there are strong reasons to believe that there is no need for the Governors to implement the rates at the immediate conclusion of this case and may not even be a need to implement the rates until the end of the Fiscal Year. Surely, the Postal Service cannot be faulted for having chosen FY 1998 as the Test Year. The selection of 1998 significantly contributed to the moderate rate increases that have been proposed, while at the same time addressing the concerns the Commission had expressed in its R94-1 decision. Under the Commission's rules, the Postal Service could have selected an FY 1999 Test Year. That would not have served any mailer interest. Similarly, the Postal Service cannot be faulted for having had better financial results than it anticipated when it submitted the case almost a year ago. Nonetheless, the Congressional mandate that the Postal Service achieve and maintain break-even "over time" (Decision in Docket R94-1 at II-30) is not intended to permit the Postal Service to increase rates and continue to accumulate surpluses when rate increases are not necessary to cover operating costs and the amortization of PYLs.

The statutory scheme accommodates this situation in which the Commission and the Governors now find themselves. Congress conferred upon the Board of Governors the power to defer implementation of rate increases precisely to enable the Postal Service to maintain break-even equilibrium "over time." Id. Thus, the Commission can and should exercise its statutory responsibilities to the maximum extent possible on the record. Then, the Postal Service Board of Governors can exercise its statutory responsibilities and powers by delaying the implementation date long enough to account for the difference between the Commission's best estimates of the Test Year revenue requirement and the point at which the Postal Service's actual financial needs require implementation of the proposed rates. It is entirely within the purview of this Commission to call to the Governors attention the facts and circumstances warranting deferral of implementation of the rate increase.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have on this date served this document upon all participants of record in this proceeding in accordance with section 12 of the rules of practice.

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DATE: April 1, 1998